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"NEVER DEPEND ON A SINGLE INCOME. MAKE AN INVESTMENT TO CREATE A SECOND

From Managing Director's Desk To Readers

SEBI'S OVERHAUL MAKES REPORTING OF MATERIAL EVENTS TIGHTER, TIMELY AND DETAILED

SEBI has issued a detailed list of material matters to be reported by listed companies and the manner of reporting them. While building on pre-existing detailed requirements, SEBI has now focused on giving even tighter deadlines of reporting and also giving a more specific list of information to be given, thus removing discretion in many places. Moreover, this time, it has also given guidance to determine whether a material development has occurred and, if so, when specifically it has taken place. This follows closely the recent amendments made to the SEBI (Listing Obligations & Reporting Requirements) Regulations, 2015 ("LODR Regulations"). These, in turn, were based on the Consultation Paper issued earlier proposing comprehensive amendments.

While the amendments to the Regulations were principle-based, the latest circular lays down the specifics and nitty-gritty of how the new requirements would have to be implemented by companies in practice.

The new requirements are more structured. The amended Regulations continue to provide for two broad categories of reporting. The first is mandatory reporting of certain events, leaving no scope for discretion to determine whether they are material or not. The second is discretionary where management has to decide whether and when a material event has taken place. However, certain minimum benchmarks are provided which, if crossed, the event would be deemed material.

The latest circular divides the specific requirements of reporting into four categories. The first gives the specific details to be reported for each material event. The circular gives a clear checklist and guidance for listed companies on what specific facts are to be reported. The second gives the timelines within which the event should be reported and this varies depending on the type of event. The overall time limit for reporting remains at 24 hours of the event.

Within this time limit, the reporting deadline ranges between as low as 30 minutes, to 12 hours and then 24 hours of the event. The third category provides guidance as to when the requirement can be said to have taken place. This too helps remove uncertainty as well as discretion. An event happens on completion of a particular milestone when there is clarity whether the event has happened or not. Finally, the fourth category gives guidance on whether a material event has taken place. The new point here is that even in this, discretion has been reduced. This was actually introduced through the amendments to the LODR Regulations, which gives specific benchmarks based on net worth, turnover or net profit/ loss. Thus, what may be material for a Rs 500 crore turnover company may not be so for a Rs 10,000 crore turnover company. This requirement too removes uncertainty and discretion.

In other words, to reframe the sequence of implementation of the new requirements, the company first has to determine whether a material event has taken place, applying the mandatory and specific requirements. If such an event has taken place, then it has to determine when the event took place. This will get the clock ticking and the 30 minutes/12 hours/24 hours deadline will be determined with reference to this time. The company has to then collect the specific and mandatory items of information to be reported. As a measure of good governance, the company may provide additional information and clarification too. Action has been taken in the past against companies that have not notified material events in time.

The new requirements thus strike a balance between mandates and discretion, quantification and judgment and, finally, achievement of milestones and timeliness of reporting.

Timely reporting of material information in a specific manner without delay helps shareholders remaining informed of events that are expected to reflect changes in performance of the company. This is in sharp contrast to the earlier days when the Board's annual report gave information that was months old, if not more than a year. Now, the information supply is constant and without delay.

The requirements of reporting of material information can be interestingly contrasted with insider trading regulations, which also deal with material information but in a different manner. The insider trading Regulations focus on keeping material, price sensitive information secret and close to the chest of the company and its insiders and to ensure that no insider illicitly profits from it. The LODR Regulations, in contrast, provide for revealing the material information so that all concerned can be made aware of at the earliest. These Regulations also ensure that the public is given authentic information straight from the horse's mouth and hence is expected to kill rumors. Both directly or indirectly control leakage of information, the former by conserving it and the later by spreading it far and wide.

However, the new requirements have become more detailed over the years. The latest version lists numerous requirements of information that have to be shared. The long list of items that are deemed material, together with the newly introduced low benchmarks for determining what is material information have resulted in numerous items required to be reported. The inevitable result is that the stock exchanges are clogged with such reporting. Add to this the fact that companies, out of a worry that some items may be on hindsight be deemed material, report events out of caution and discretion. This further adds to the information overload. Unless a person is closely observing and reading in minute detail each of the information supplied, she may miss the really important ones in the long list. However, in a regime that focusses more on disclosure than on micro-regulation of companies, this is inevitable. This is also reflected in the fact that prospectuses and annual reports now run into hundreds of pages.

One more area of concern is the short time available to companies to determine whether a material event has happened, when it has happened, collecting the items of information to be reported and then reporting it within 30 minutes, 12 hours or 24 hours as the case may be. Considering that numerous events keep taking place in a company, this may become a challenging task. SEBI's answer to this is that the company should ensure that there is adequate education at the lowermost level, as they are the first witnesses of developments and so that they can quickly pass on information up the corporate hierarchy. However, this is easier said than done. Awareness, understanding and implementation of such complex regulations require a mix of legal knowledge and senior level judgment. Laying down such systems would also come at a cost.

To conclude, the new requirements are well-meaning. There would be added efforts but then these are the costs of listing and seeking monies from the public and running a company by following good corporate governance practices. On the other hand, I also feel that the list of matters deemed to be material could be trimmed down. They may not be reduced to the level of SOS items only. But, for example, the freshly lowered quantified benchmarks could be revisited and even the items that are mandatorily deemed to be reported. This, however, is a moving goal and can be the subject of the next review and consultation paper after the implementation of the new requirements is reviewed in practice.

Salil Shah

Managing Director

Lakshmishree Investments & Securities Pvt. Ltd.

Look What Our Research Analyst Has To Say...

Nifty on the expected lines is trading around all time high and facing some heat. We expect a pullback in the month of august to test 19350 odd levels which will be an opportunity to buy in the long term structural bull market. Post dips towards 19350 we expect the markets to rally to fresh all time high but in the last week of August or first week of September.

GROWTH IN THE IT SECTOR WILL BE SLOW

The information technology (IT) industry is making a comeback in terms of popularity. But the Q1FY24 (April-June 2023) financials and the guidance received don't seem to justify this. Management guidance by industry leaders — Tata Consultancy Services (TCS), Wipro, HCLTech, and Infosys — can be termed mildly, or at best cautiously, optimistic. However, investors have pushed up the IT index by 5 per cent in the past week after absorbing available Q1FY24 results and guidance.

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This could be classified as a relief rally because worse was expected. Some investors may also be simply over-optimistic, given the general momentum. The panic about macro weakness across North America and the European Union has declined. That's good news. Churn has reduced. But there's little visibility of strong rebound. Clients are clearly holding back on discretionary spending and avoiding projects without immediate return on investment.

In terms of new trends, while the initial adoption of generative artificial intelligence (AI) seems promising, the enterprise adoption of this new technology seems much more measured than the popular hype. Both Infosys and TCS have started pushing into this space. Macroeconomic challenges will continue to be a drag on near-term growth across the industry. The deal pipeline for now seems healthy with decent order inflows. But at best, the IT companies are maintaining their prior FY24 guidance and they have warned that orders will translate into revenue growth only late in FY24. Margin pressures were apparent across the Q1FY24 results, and may persist until well into the second half of FY24.

Infosys has cut the constant-currency revenue-guidance band for FY24 to 1- 3.5 per cent (from 4-7 per cent) despite saying Q1 was stronger than expected and the company was receiving orders. Infosys has also deferred wage hikes for some employees. HCLTech maintains its prior guidance despite a relatively weak Q1FY24. Although it has deferred most scheduled wage hikes, there is cause for optimism in terms of strong order inflows. TCS also says the outlook has not changed much since Q4FY23.

Wipro had an uninspiring Q1 and offered weak revenue guidance, indicating a potential drop in revenue in Q2FY24. It also warned that margins might come under pressure in the second half when it intends to institute deferred wage hikes. While attrition rates have dipped across large firms, the headcount declined quarter-on-quarter. TCS added a net of 523 employees to its headcount of 615,000, while Wipro reduced its staff strength by 8,812. Infosys saw a reduction of 6,940. The decline in HCLTech was at 2,506.

Notably, Infosys has not released a hiring target for FY24, which is a break from normal practice and indicates caution. Infosys also referred to the reduced volume of work, especially in the banking and financial services industry, and also in telecom.

All the companies referred to better cost-efficiencies and better workforce utilisation. Infosys also referred to the transformative impact of AI within the company's internal processes where 40,000 employees (out of 336,000) are being trained in handling AI. However, the disconnect between lukewarm guidance and the stock market response was stark. These companies are bellwethers with exposures across all geographies and verticals. It is thus likely that smaller IT services firms may be hit harder since they have fewer resources and are more skewed in terms of exposure.

Anshul Jain

Research Analyst

Stocks To Watch

1. ACC LIMITED

ACC Limited is a prominent player in the Indian building materials industry. Its history dates back to 1936 when ten cement companies merged to form the company, making it the country's first notable merger. The company's founder, F E Dinshaw, played a crucial role in establishing the Indian cement industry. Despite facing competition and challenges, ACC thrived and became a leading cement giant.

Today, it is part of the Adani Group and is known for its innovative research and product development. ACC operates 17 modern cement factories, 90 ready mixed concrete plants, and has a vast distribution network with numerous sales offices across India.

Particulars

Bloomberg	JKLC IN
Market Capitalisation	₹ 36,598 Cr.
52 Week Range H/L	₹2,785 / ₹1592
Equity Capital (Cr.)	₹188
Avg Daily Volume (6m)	763824
Return On Equity	7.06%

Shareholding Pattern

In (%)	Dec-22	Mar-23	June-23
Promoter	56.69	56.69	56.69
DII	16.74	17.59	18.1
FII	11.95	10.05	9.98
Others	14.62	15.67	15.23

Profit & Loss Statement

Y/E March (₹ Cr.)	FY 22	FY 23	FY 24E	FY 25E
Net Sales	**16152**	**22210**	**19434**	**21288**
Other Operating Income	0	0	0	0
Total Income	16152	22210	19434	21288
Raw Material	2867	5454	5335	5709
Power & Fuel	3365	5743	3991	4270
Freight & Forwarding	3823	5140	4291	4634
Employee Benefit Expenses	836	1036	705	733
Other Expenses	2263	2912	2280	2462
EBITDA	**2998**	**1925**	**2832**	**3479**
Other Income	207	342	271	319
PBIDT	3205	2267	3104	3799
Depreciation	601	840	800	841
Interest & Fin Chg.	55	77	77	85
E/O Income/ (Expense)	55	0	0	0
Pre-Tax Profit	2495	1348	2227	2872
Tax Provision	643	317	573	722
RPAT	**1851**	**1031**	**1654**	**2150**
Minority Interests	0	0	0	0
Associates	12	16	16	16
APAT after EO Item	**1863**	**1049**	**1670**	**2166**

Balance Sheet

Y/E March (₹ Mn)	FY 22	FY 23	FY 24E	FY 25E
Total Assets	**21,039**	**20,544**	**22,016**	**24,089**
Net Block	7,995	9,196	9,764	9,988
CWIP	1,245	1,684	484	484
Investments	131	145	145	145
Wkg. Cap. (exclu. Cash)	-142	1000	490	540
Cash / Bank Balance	7,524	415	3,031	4,720
Misc. Assets	4,286	8,104	8,103	8,212
Capital Employed	**21,039**	**20,544**	**22,016**	**24,089**
Equity Capital	188	188	188	188
Reserves	14,121	13,950	15,432	17,410
Minority Interest	3	3	4	4
Borrowings	0	274	274	274
Def Tax Liabilities	216	178	178	178
Other Liabilities and Provision	6,511	5,950	5,941	6,036

Cash Flow Statement

Y/E March (₹ Mn)	FY 22	FY 23	FY 24E	FY 25E
Profit Before Tax	**2506**	**1203**	**2243**	**2888**
Depreciation	601	841	800	841
Interest Expenses	55	77	77	85
Non-Operating / EO Item	-214	-331	-287	-335
Change in W/C	130	-2671	1710	-50
Income Tax	-286	-404	-573	-722
Operating Cash Flow	**2792**	**-1284**	**3970**	**2707**
Capital Expenditure	-1175	-2105	-2560	-1064
Investments	0	0	0	0
Others	177	215	1471	319
Investing Cash Flow	**-998**	**-1890**	**-1089**	**-745**
Borrowings	0	0	0	0
Interest Expenses	-32	-60	-77	-85
Dividend Paid	-263	-1089	-188	-188
Others	0	0	0	0
Financing Cash Flow	**-295**	**-1149**	**-265**	**-273**
Change In Cash	1499	-4323	2616	1689
Opening Balance	5849	7367	257	2873
Closing Balance	7348	3044	2873	4562

Our Take...

The company experienced a significant increase in volume growth, reaching 9.04 million tonnes per annum (mtpa), a YoY growth of 24%. This growth was driven by increased production of blended cement and improved efficiency. The company maintains its market leadership in key markets and is expected to experience further volume growth with the commercialization of the Ametha integrated unit. The company has implemented cost optimization measures resulting in a 12% reduction in overall cost, leading to an improved EBITDA margin from 9.5% to 14.8% YoY. Ongoing business initiatives are expected to further reduce costs, expand margins, and improve EBITDA/tonne to Rs 920 in FY25. The stock's valuation is attractive as it is trading below the industry average EV/EBITDA multiple. The sector outlook is positive, and the company anticipates sustained demand and strong volumes due to increasing construction activities. The company expects EBITDA to continue to improve through operational excellence initiatives.

Outlook & Valuation

The company has plans to establish a new greenfield integrated unit in Ametha, Madhya Pradesh. This move is expected to increase demand in the central region by the second quarter of the financial year 2023-2024. The rise in infrastructure development spending, including schemes for affordable housing, roads, railways, and others, is also driving up the demand for cement. The company anticipates better synergies with other group companies, which will contribute to its future growth.

The stock is currently considered attractive at 11x and 8x FY24E/FY25E EV/EBITDA and EV/tonne of $100 and $95, respectively. We recommend to BUY the stock with a target price (TP) of Rs 2623.

2. INDIAN HOTEL

The Indian Hotels Company Limited (IHCL) is a renowned hospitality company part of the Tata Group, managing hotels, resorts, palaces, spas, safaris, and in-flight catering services. Founded in 1902, its flagship hotel is the Taj Mahal Palace Hotel in Mumbai, India's first five-star hotel. IHCL operates under various brand names like SeleQtions, Vivanta, Ama, Ginger, and more, offering dining options, holiday packages, and wedding planning services.

It has a global presence in countries including India, Maldives, UK, US, UAE, and South Africa. Headquartered in Mumbai, IHCL also offers loyalty programs like Taj InnerCircle and Taj Experiences Gift Cards.

Market Data

Bloomberg	IH IN
Market Capitalisation	₹ 56,042 Cr
52 Week Range H/L	406 / 262
Equity Capital	142 Cr
Return On Equity	12.7%
3M Daily Avg Trd. Val (₹ m)	63.1

Shareholding Pattern

In (%)	June-23	Mar-23	Dec-22
Promoter	38.19	38.19	38.19
FIIs	21.64	18.24	19
DIIs	23.76	27.29	26.51
Others	16.41	16.28	16.3

Profit & Loss Statement

Y/E March (Rs Mn)	FY 22	FY 23	FY 24E	FY 25E
Net Sales	**30562**	**58099**	**65130**	**73271**
Change (YoY, %)	94.0	90.1	12.0	12.5
Operating Expenses	-26515	-40054	-44353	-48725
EBITDA	**4048**	**18046**	**20776**	**24546**
Change (YoY %)	-211.9	345.8	15.1	18.1
Margin (%)	13.2	31.1	31.9	33.5
Depreciation	-4061	-4161	-4875	-5068
EBIT	**-13**	**13885**	**15901**	**19478**
Interest Paid	-4277	-2361	-801	-525
Other Income	2552	2389	2458	2531
Pre-Tax Profit	**-1738**	**13914**	**17559**	**21485**
Tax	358	-3232	-4168	-5156
Effective Tax Rate (%)	20.6	23.2	23.7	24.0
Minority Interest	-425.7	814.0	500.0	500.0
Net Profit	**-1806**	**11495**	**13891**	**16829**
Exceptional Items	-	-	-	-
Adjusted Net Profit	**-1806**	**11495**	**13891**	**16829**
Change (YoY %)	-78.9	-736.5	20.8	21.2
EPS	-1.3	8.1	9.8	11.8
Dividend Per Sh.	0.4	1.0	1.5	1.5
Dividend Payout (%)	-38.4	15.1	18.7	15.4

Balance Sheet

Y/E March (Rs Mn)	FY 22	FY 23	FY 24E	FY 25E
Shareholders' Funds	**70623**	**79820**	**89611**	**102341**
Share Capital	1420	1420	1420	1420
Reserves & Surplus	69202	78399	88191	100920
Total Debt	**23628**	**12816**	**3204**	**2098**
Other Liabilities	20303	25144	24535	23784
Current Liab. & Provision	**10413**	**12307**	**13380**	**14476**
Current Liabilities	7503	9048	9957	10860
Provisions	2909	3259	3422	3616
Total Liabilities	**54344**	**50267**	**41118**	**40358**
Total Equity & Liabilities	**130896**	**136688**	**137330**	**149299**
Net Fixed Assets	59192	60605	59459	58098
Investments	5166	4826	5212	5577
Other Non-Curr Assets	39797	45353	45982	46763
Current Assets	**26741**	**25903**	**26679**	**38861**
Inventories	1008	1092	1212	1333
Sundry Debtors	2553	4465	4911	5304
Cash and Bank	11878	10534	6717	15328
Loans & Advances	865	844	945	1040
Total Assets	**130896**	**136688**	**137330**	**149299**

Cash Flow Statement

Y/E March (₹ Mn)	FY 22	FY 23	FY 24E	FY 25E
Pre-Tax Profit	-1738	13914	17559	21485
Depreciation	4061	4161	4875	5068
Tax Paid	53	-2543	-4793	-5929
Change in W/C	-17412	-79	405	487
Other Operating Capital	-	-	-	-
Cash Flow From Operations (a)	**-15037**	**15452**	**18046**	**21110**
Capital Expenditure	-4323	-5573	-3727	-3708
Change in Investments	228	340	-386	-365
Other Investing Activities	-	-	-	-
Cash Flow From Investing (b)	**-4095**	**-5233**	**-4113**	**-4073**
Equity Raised / (Repaid)	42413	-	-	-
Debt Raised / (Repaid)	-1036	-10812	-9612	-1105
Dividend (incl. tax)	-693	-1733	-2599	-2599
Chg. In Minorities	-841	1485	500	500
Other Financing Activities	-10369	-502	-6039	-5221
Cash Flow From Financing (c)	**29474**	**-11562**	**-17750**	**-8426**
Net Change in Cash (a+b+c)	**10342**	**-1344**	**-3818**	**8612**

Our Take...

In the first quarter, IHCL (Indian Hotels Company Limited) recorded a 15.8% YoY increase in net sales, reaching Rs14.7 billion. The strong performance was driven by domestic same-store RevPAR outperforming the industry by 55%. International operations also showed positive growth, with a 65% occupancy rate, marking an 11% expansion compared to the previous year. IHCL's asset-light strategy contributed to a 20% YoY growth in Management Fee income.

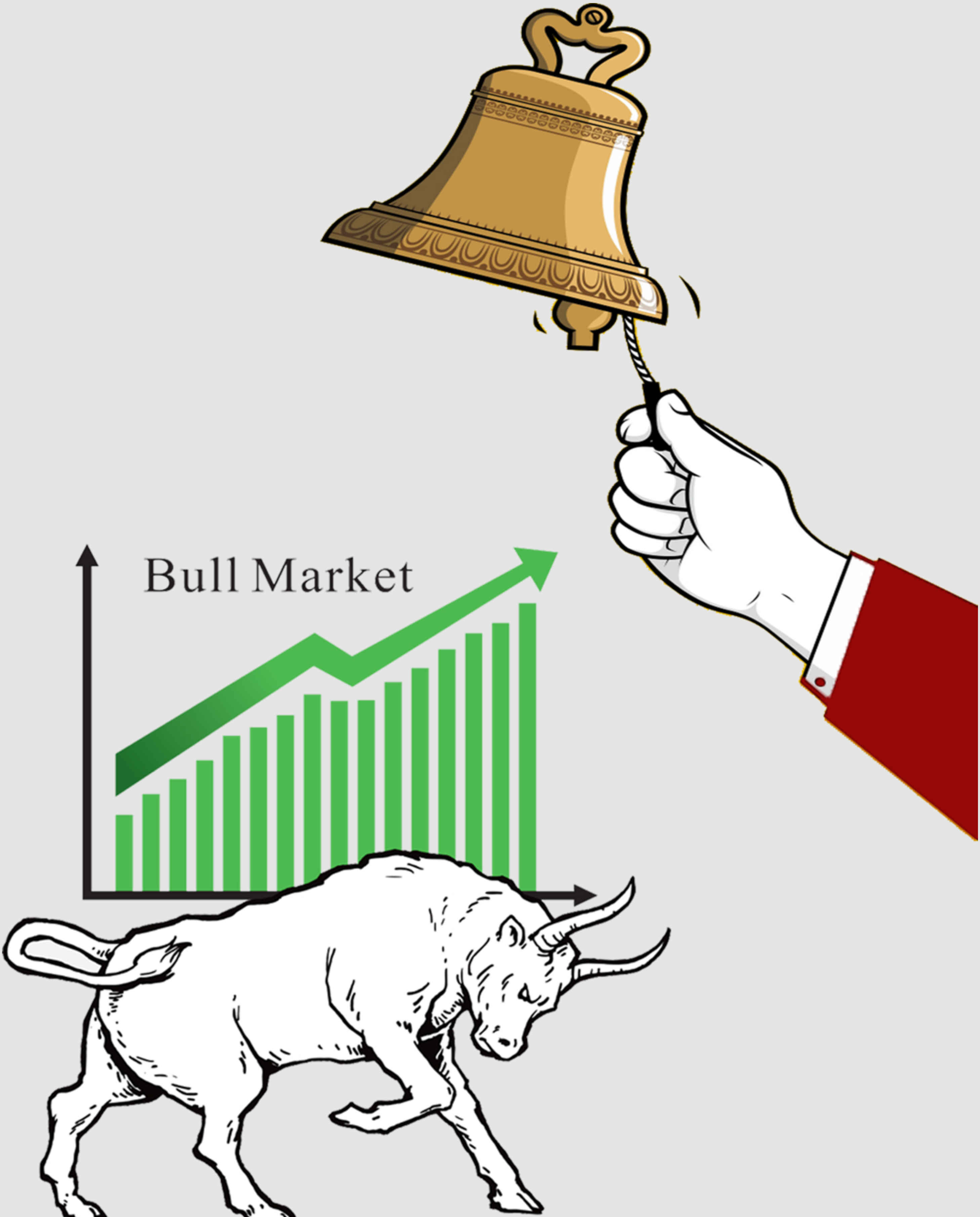
The company is expanding its presence with the opening of Ginger Santacruz and plans to renovate five Ginger hotels in FY24. With 249 hotels across 125+ locations in 30+ states and UTs, IHCL is continuously signing new hotel deals. Qmin, Tata New, and Ginger reported promising performance, while the international business segment achieved net sales of Rs356 crore and a PAT of Rs8 crore in Q1FY24. The estimated capex for FY24 is around Rs600 crore.

Outlook & Valuation

Indian Hotels Company Ltd.'s (IHCL) Q1FY24 result was in-line with our estimate on net sales front, while EBITDA/PAT were below our forecast. Healthy demand supported occupancy and ADR, which resulted in healthy net sales growth. The management reiterated its guidance of adding 20 hotels in FY24E.

We believe demand will remain buoyant in upcoming quarters aided by the G20 summit and Cricket World Cup. Qmin, Ama, and Chambers are growing at a healthy pace and should contribute to earnings in a meaningful way in the near term. Net sales increased by 15.8% YoY to Rs14.7bn, while EBITDA came in at Rs4.1bn, healthy growth of 8.5% YoY. Net profit stood at Rs2.4bn, higher by 38.8% YoY. We have broadly maintained our earnings estimates for FY24E/FY25E. We recommend BUY on this stock with a Target Price of Rs 512.

This May Impact Your Investments!!



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Why Sovereign Gold Bonds Have Become A Preferred Financial Asset

Equity markets continue to touch new highs even as earnings growth in India slows down due to global issues. Some investors are getting jittery and looking for other investment avenues. With rising uncertainty regarding inflation, interest rates and the outcome of the ongoing war between Russia and Ukraine, gold is the first port of choice.

Though Indians have been among top two importers of gold in the world, consumption has been mostly in the form of pieces of jewelry. There are a small percentage of investors who prefer to buy gold in the form of coins, biscuits, or bricks.

However, since the government introduced Sovereign Gold Bonds (SGB) in 2015 the concept of gold buying in non-physical format was introduced. Though Gold Exchange Traded Funds (ETF) was introduced in 2007, they did not gain much traction in the first decade of its launch.

After the initial tentative steps both these forms of investment in gold have picked up.

There are five SGBs launched every year, and the first one in the current fiscal garnered investment worth Rs 4,604 crore, equivalent to 7.77 tonnes. This investment follows a record 100 tonnes of SGB collection in FY23.

SGB was introduced in the 2015-16 Union Budget and are government securities denominated in grams of gold issued by the RBI. The scheme has an eight-year lock-in and the holder gets a small interest payment on their holding.

Since its launch 64 tranches of SGBs have been issued through 11.04 crore units. After a small spike during the pandemic, SGB investments tapered down only to pick up in the first tranche of the current fiscal.

Gold is attracting investment partly because of its steady rise. Despite the pandemic and multiple headwinds, gold prices have continued to rise.

When the first issue was launched in 2015 it was for Rs 2,684 per gm which rose to Rs 5,926 per gm in the recent issue. The RBI fixes the nominal value of the bonds based on the simple average of the closing price of gold of 999 purity for the last three business days of the week preceding the subscription period.

Almost all SGB issues were either close to the previous issue or higher than it. Since SGBs have a lock-in period (withdrawals are allowed with certain conditions) mostly the instrument witnesses inflows.

This, however, is not the case with Gold ETF. Gold ETFs are units representing physical gold, where one gold ETF unit is equal to 1 gram of gold and backed by physical gold of 999 purity.

Fund flows change with market mood. From November 2022 to January 2023, Gold ETFs saw a cumulative outflow of Rs 673 crore. Calendar 2022 was a bad year for Gold ETF with a net inflow of Rs 459 crore, a fall of 90 percent over Rs 4,814 crore over the previous year. Today there are 46.94 folios of gold ETFs across various asset management companies.

Despite being an early entrant Gold ETFs have not picked up as much as SGB. Indians have traditionally considered gold to be an asset that stores value. The form of purchasing may have changed, but SGB's success indicates an increasing appetite for non-physical gold.

At 100 tonnes (FY23 SGB investments) gold bonds are perhaps making a dent in the physical market. FY23 saw imports of physical gold drop by 24 percent to 677 tonnes from 878 tonnes a year earlier. This helps the government to manage its current account deficit.

Alternate investment instruments are healthy for the development of the overall financial market in the country. If the trend of increasing investments through SGB continues, gold as a financial asset will shift from the physical form that Indians have been using for generations to the electronic form of holding it.

GST On Online Games: A Measure To Keep Youth From Harm And Debt Trap

The Goods and Service Tax (GST) Council recently decided to impose a 28 percent tax on online games. Although no objection has been noticed from the players on online games apps, the app companies which run these games raised objections. These app companies claimed that they would suffer losses due to the imposition of GST on online games. A few days back, 180 gaming companies asked the GST Council to reconsider its decision.

Gaming companies argue that the proposal to levy GST on the full deposit amount will reverse the growth trajectory of this 'industry'. Not only will the existing companies suffer, but also the existence of new smaller players will become difficult. These companies further claim that fresh investment by domestic and foreign investors in this sector will be discouraged and that the entire startup ecosystem will be affected by this decision.

Though the government did not give any argument for and against gaming apps while explaining this decision to impose GST, it is a fact that there is a great deal of concern in various circles due to the increasing addiction of youth to these online games and the anomalies and crises caused by these games. The government is well aware of this menace. It must be noted that a total of 40 million people play these online games, and 10 million do it regularly.

The government says that so far only 2-3 percent GST is levied on these games, which is less than 5 percent GST on food items consumed by the common man. By imposing 28 percent GST, the government is expected to fetch a revenue of Rs 20,000 crore.

Matter Of Concern

Many types of online games have emerged in the last few years. Even renowned personalities from the sports and entertainment sector are promoting these apps run by many big companies. However, these same ads also carry a quick warning, 'Play these games carefully, they can be addictive'. In fact, today our youth are getting trapped in the clutches of apps and games endorsed by these celebrities. For some time, due to the expansion of the internet and mobile phones in the country, this real money gaming 'industry' has expanded more and its scope is increasing fast.

Many online and app-based games including share-trading-related games, crypto-based games, rummy, ludo and virtual games (fantasy sports) are called 'real money games' as these games are played for money or awards. Some of these games are said to be skill-based and some others are based on chance (i.e., gambling). Be it chance-based or skill-based, all online games have expanded rapidly and the companies promoting these apps and websites are making huge profits. But the matter of concern is that due to these games, the future of our youth is endangered.

Since the advent of these games, many young people have lost their lives after getting into a debt trap. It has to be understood that the chances of winning in these games are very low, yet due to gambling addiction, the young start taking huge debts and their families are ruined. Today, apps like Dream 11 have become famous all over the country due to endorsement by big cricket personalities. Apps like Ludo are being endorsed by big names in the entertainment industry like Kapil Sharma and many other celebrities. Most of the youth who commit suicide after getting trapped in these apps are between 18 and 25 years of age, and include students, migrant labourers and businessmen.

Skill Or Chance

In the context of Dream 11, most of the courts have justified it by saying that it is not gambling but a game of skill. Despite that six state governments have banned or not allowed such virtual cricket platforms. Similarly, Andhra Pradesh chiefminister YS Jaganmohan Reddy has requested a ban of 132 apps.

Even if it is assumed that there is no chance element in a virtual cricket game and hence it is not gambling, but some sports psychologists believe that virtual cricket is actually gambling and can lead to pathological gambling behaviour. Companies involved in this business are not willing to accept that it can lead to addiction and they argue that the average deposit amount is very little. But the reality is different from this. This statement is proved wrong by the fact that those who committed suicide were in huge debt of lakhs of rupees after losing in these games. So, it is not fair to believe the claims of these virtual sports app companies. The most important thing is that there is no regulatory authority regarding these games, and this business is only self-regulated. There is a huge difference between the claims and reality of the companies involved in this business.

Courts are yet to decide whether so-called skill-based games involving money bets are gambling, but any game involving an element of chance is gambling and may not be legal under the law of the land. It is also seen that many apps are running pure gambling platforms in the garb of skill-based games. Importantly, these apps are heavily funded by foreign investors, especially Chinese investors, and their sole purpose is to make people addicted to gambling. The design of these apps itself is addictive. Not only this, but by tampering with the software of many so-called skill-based games, customers are being fooled and looted. Not only the 276th report of the Law Commission of India, but even the Supreme Court has also commented that the results of these skill-based games can be influenced by mechanical tampering.

Effect Of GST

The government levies GST on all goods and services except agricultural commodities. There are certain goods and services that cannot be allowed into the country. Activities like gambling, prostitution, theft-robbery etc, are legally prohibited in our country. Apart from this, there are some things whose production and consumption are discouraged and it is the social responsibility of the government to minimise them. Tobacco and liquor are classic examples in this regard, and maximum tax has been levied on tobacco products and liquor in the country. In the budget for the year 2023-24, the finance minister imposed an additional tax on cigarettes, over and above the highest rate of GST. Online real money games are yet not properly defined, whether it is 'gambling' or 'games of skill'. But since there is a high possibility of losing money in these games, if such games are taxed less, it would go against social welfare.

It is absolutely an appropriate step by the GST Council to impose the tax on these virtual games at the maximum rate, as it is a kind of social evil. No civilised society can accept situations like increasing debt and suicide among the youth due to the growing addiction towards these games and the huge financial loss caused to them. Obviously, the highest rate of GST imposed on deposit amount on these games by the government is an indication that the government is sensitive to the miseries of the youth who lack information and maturity and are squandering money in gambling through apps or so-called skill-based games.

Sheela Foam: Will Kurlon And Furlenco Make Good Bedfellows?

Mattress company Sheela Foam's management appears to believe in grabbing opportunities that come its way. But deals, good as they may be, cost money and as the management itself said, integration of work cultures will be crucial to success.

There are other aspects to be considered too, such as financing, but the most important one is likely to be the attention span of management. There's an existing business it must run, then do the hard work of integrating the Kurlon business and reap benefits such as cost savings, and then also figure out how to make the Furlenco acquisition a success.

Sheela Foam, known for its Sleepwell range of mattresses, is paying Rs 2035 crore to acquire a 95 percent stake in Kurlon, the famous coir-based mattress company. It's also investing Rs 300 crore to buy a 35 percent stake in Furlenco, a startup best known for its furniture rental business. If it decides to buy out the minority stake in Kurlon or exercise its option to take majority stake in Furlenco, then its financial commitments could increase.

It plans to use the cash on its balance sheet—around Rs 750 crore as of March 31, 2023, at the consolidated level—and then raise debt and equity to fund the rest. It already has Rs 460 crore worth of loans, and that could act as a fetter while raising debt. Still, with a net worth of Rs 1600 crore it has ample headroom to raise debt, although it would put some strain on its financials in the near term. Too much dilution would worry investors and debt can be repaid easier compared to buying back shares to reduce capital, so that's the preferred mix.

The mattress market is a fragmented one and this deal consolidates the top companies' stake. Kurlon adds 8 percent to Sheela Foam's 13 percent stake in the mattress market, taking it to 21 percent. The next five players have shares of between one and 5 percent each. The acquisition lends scale, adding Rs 800 crore in revenue in FY23 to Sheela Foam's Rs 2873 crore, and an almost invincible lead in the organised market. If Kurlon was in play, an aggressive PE-backed competitor could have become a pain in the neck for Sheela Foam.

The opportunity in the deal lies in reviving Kurlon's sales to the Rs 990 crore levels they were in FY20. COVID affected its performance and EBITDA margin has also fallen to a low 2.5 percent compared to Sheela Foam's 10.4 percent. The first big challenge will be cultural, with one being a North-based company and the other a South-based one, and even if that's not a big challenge, different management styles of the promoters need to be reconciled. The usual method of putting together an integration team and hiring consultants is being done. But what really matters is for the new management to be on the ground and resolve differences as they arise.

The financial benefits will come from a few areas. One pertains to the structural changes that caused problems for Kurlon, these will be reviewed. Another is on pooling of services such as logistics, raw material procurement (4 percentage points of potential cost savings for both functions) and possibly even some corporate functions. Optimised manufacturing could yield a 20 percent improvement in utilisation levels, according to the management.

The bigger benefits can come in the front-end, as there is not much overlap in the markets they are in and the products they offer. Sheela Foam is strong in the North and West while Kurlon is strong in the South and East. One specialises in foam-based and the other in coir-based mattresses.

But there is the question of integrating the front-end—the shops where the products are displayed and sold—in a manner that does not confuse the customer and salespeople. The management recognises this, which is a good sign. A poor outcome will be consumers switching over from one to the other, which only cannibalises sales, but an optimal one is where new customers are acquired for both brands. The management has said it will unveil these plans in a few weeks and investors should keep a watch to see if they appear sensible.

Initially, there may be some impact of the acquisition on earnings but to justify the dilution in equity and debt costs, Kurlon's profitability needs to get back to the 12 percent levels soon. This should then lead to improved earnings growth and cash flows, which can then also help in paying down debt taken for the acquisition. The acquisition is reasonably priced but that's also because of the low operating profitability and challenges that lie ahead.

If it works, then Sheela Foam's sales to market cap ratio of 4.2 times means if Kurlon reaches sales of Rs 1000 crore as planned, it should be valued at twice the acquisition cost. Sheela Foam's shares have run up since rumours of the acquisition made the rounds and if they have not fallen even after the acquisition was announced, then this valuation opportunity could be the main reason behind it.

But then comes the Furlenco acquisition. It's a startup that's been in financial trouble and has also been unable to service new orders. Its debt levels have risen sharply. Sheela Foam appears to think these problems are solvable and there's a big opportunity left to exploit. Half the consideration of Rs 300 crore will be used to repay its debt and the rest will be used to fulfil orders.

The company rents out furniture to customers. The business model involves making or buying the furniture, then renting it out, which will pay back with profits over the life of the rental. But this also means to get new business, the company needs new furniture and working capital to fulfil orders. That has got jammed and Sheela Foam aims to free it up. It also sees potential in other parts of Furlenco's business model such as its existing premium furniture brand and has plans to expand gradually into a full-fledged furniture business.

What's common to the furniture and mattress businesses is that unorganised players have a large share of the market. The second common factor is that customers who buy mattresses would typically be seeking to buy furniture as well such as those buying a new home or renovating existing ones. The odd ones out will be those who are replacing their old mattresses. Cross-selling opportunities can be sought out. There is a business linkage here too as Sheela Foam plans to supply foam to meet Furlenco's requirements.

Sheela Foam plans to increase its 35 percent stake to 44 percent at the same price and has options to increase it further. Once Furlenco turns around its operations and financials, Sheela Foam may seek to acquire majority stake.

While the acquisition value is relatively small, the risks here are greater. The furniture market may be a much larger one than the mattress business but it's also very different. Within that, the rental business is a niche. Startups are accustomed to using capital to acquire customers and revenue and then use more capital to scale up. What Sheela Foam's investors would like is for the rental business to become self-sustaining. Growth could turn slower. More than that, plans to expand into furniture will also mean more investments. Therefore, the capital needs from this business may continue, even as there may be a long path ahead to attain sustainable revenue growth and profitability. The visibility on this business and Sheela Foam's exposure and capital commitments to it need to be watched by investors.

Overall, Sheela Foam has a lot on its plate to execute in the next few years. That's why management attention or 'bandwidth' as it's called in business jargon, is the crucial ingredient that will determine if these acquisitions pay back exponentially or become a millstone around its neck.

Why Financial Conditions Remain Loose Despite Rate Hikes

Don't fight the Fed' is a well-known market adage. The reason is rather obvious. Fed policy determines liquidity in the economy and with it, the cost of capital. And if we stretch the point a bit, Fed policy also affects the global supply of liquidity and the US dollar, the currency in which much of world trade happens. Fed policy reverberates around global markets.

Fighting the Fed

But that was then. More recently, the markets seem to be more interesting in fighting the Fed. Why else are the markets higher now than where they were in March 2022, when the Fed's tightening cycle began, in spite of the Fed Funds rate being hiked by over 5 percentage points since then? While everybody has been hoping for a soft landing for the US economy, the soft landing in the US markets happened in October last year.

That is also true of other equity markets. The FTSE 100 is 10 percent above its October lows. The Reserve Bank of India started hiking rates from May 2022 and the Nifty made a low in mid-June last year, but it's now up 28 percent from those lows, despite the repo rate going up from 4 percent to 6.5 percent.

The standard answer is that the markets are forward-looking. Having fallen once the rate hikes began, they soon began to look forward to a time when central banks will pause and then start cutting rates to support the economy.

Years of developed country central banks flooding the global economy with liquidity led to the perception that they will always be around to bail out the markets. 'Don't fight the Fed' is an adage from another era, one in which they removed the punch bowl when the party got going. These days, the market remembers that the Fed has instead spiked the punch bowl with monetary methadone, sending asset prices to new highs. Is it any wonder then that markets are sceptical about monetary tightening?

Loosening financial conditions

The upshot is a loosening of US financial conditions despite the rate hikes and in spite of quantitative tightening. Definitions of 'financial conditions' vary. But the Chicago Fed Adjusted National Financial Conditions Index is now lower than in March 2022, before the Fed started to tighten. And the Fed's new index, the FCI-G, or the Financial Conditions impulse on growth, at end-June 2023 at its lowest level since August 2022. The result is that firms can raise funds from the markets and even high yield spreads have come down sharply from the highs reached in March this year.

What is going on? Fed chair Jerome Powell essayed an explanation at his post-FOMC meet press conference. He said, 'we know that in the modern era, financial conditions move in anticipation of our decisions and that has clearly been the case in this cycle. So in a sense, the clock starts earlier than it used to.' Powell is saying that the markets now discount Fed policy and financial conditions are loosening in anticipation of the end of rate hikes and a start to rate cuts. He also said, 'in principle, that could mean that if financial conditions get looser we have to do more. But what tends to happen though is financial conditions get in and out of alignment with what we're doing, and ultimately over time we get where we need to go.' That could be read as a signal that they have no intention of doing more to tighten financial conditions.

There are other explanations why monetary tightening hasn't had more of an impact. Some analysts say that recent quantitative tightening has scaled back only a small portion of the tsunami of liquidity unleashed by central banks during the pandemic. Others point out that government spending remains high.

A recent IMF note says that a prolonged period of extremely loose financial conditions may have dulled the transmission of monetary policy to financial conditions. It points out that the share of fixed-rate mortgages with low rates is very high in the United States, because borrowers refinanced those loans when rates were very low. Similarly, firms took advantage of exceptionally low borrowing costs and ample liquidity to extend their debt maturities. The IMF note says, 'In both cases, this may have dampened the effectiveness of monetary policy tightening, as many mortgage holders and companies have only begun to face higher borrowing costs, thus contributing to the continued strength in labour markets and aggregate demand.'

Whatever happened to the recession?

The loose financial conditions have cushioned the US economy, so much so that its GDP rose at an annual rate of 2.4 percent in the June 2023 quarter, compared to 2 percent in the March quarter. The Atlanta Fed's GDP Now estimate for the third quarter of 2023 is 3.5 percent. The IMF has recently upped its estimate of global growth.

At the same time, inflation is easing. Supply-side inflation in goods has disappeared and it is the resilient services sector that is pushing up prices.

As for the feared geopolitical backlash, in spite of the economic friction with China, US imports from China continue to exert a downward pull on inflation—year-on-year, the price index of US imports from China fell 2.3 percent in June 2023.

The hope is that with excess savings built up during the pandemic being drawn down and with higher interest rates, consumption will slow. Indeed, the Conference Board has pointed out that the Q2 US GDP data show that consumption growth cooled for the quarter, but improvements in business investment growth more than offset this.

Markets simply do not believe central banks will have the guts to rock the boat, nor do they think they have any need to. Then there's the AI bubble, which still has a long way to run. And if inflation is coming down and growth is holding up, that immaculate disinflation is great for markets.

The risk

The risk is of more persistent inflation. A 'FEDS notes' paper published early this month said inflation may remain more persistent. The paper said, 'Experience in 2022 and early 2023 suggests that the Bayesian approach with notable inflation persistence provided good guidance on the inflation outlook. Models using this approach suggest core CPI inflation may remain above 3 1/2 percent through 2024, higher than professional forecasters expect.'

The IMF points out that such a scenario where underlying inflation continues to be sticky and declines only slowly is a risk. The IMF Note says that tighter monetary policy for longer than currently priced by financial markets may be needed, resulting in higher real interest rates. This could hurt investor sentiment as market participants reassess the inflation and policy outlook, leading to a re-pricing of risk assets, especially as there is very little margin of error in the markets at these levels.

But the markets are betting that the US authorities will do their best to ensure the Goldilocks economy continues in an election year.

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